

Case Study Name	Procurement and cash fraud in construction of multi-purpose sports facility
Description	<p>The purpose of the project was to build a multi-purpose sports facility with the overall objective of providing youth and children after and out-of- school activities, which could also contribute to improved health and the prevention of substance abuse. The project included the following activities and results:</p> <ul style="list-style-type: none"> - Construction of a football playground; - Construction of three tennis courts; - Project promotion; - Management. <p>The fraudulent actions took place during the project implementation (April 2008 – December 2009).</p>
ESI Fund(s) concerned	No ESI Fund/s was/were concerned. The project was funded by European Economic Area (EEA) and Norway Grants during the Financial Mechanisms 2004-2009
Irregularity type	<ul style="list-style-type: none"> - Procurement fraud: conflict of interest, coordination of bids, price inflation, noncompliance of construction works with contract specifications and construction permit, missing procurement files. - Cash payments fraud: missing audit trail, faking of account bank statements.
Reporting mechanism	Following allegations of fraud, the Donors of EEA and Norway Grants (i.e. Ministries of Foreign Affairs of Iceland, Liechtenstein and Norway) requested the Financial Mechanism Office (FMO) to perform ex-post audits. The audits revealed several shortcomings and irregularities, which led the Donors to conclude that fraudulent intentions lay behind and/or fraudulent actions took place in the course of the project.
IMS reporting	<p>No</p> <p>(Based on findings detected by ex-post audits, the irregularity and fraudulent cases were reported to the Donors of EEA and Norway Grants).</p>
Red flag(s)	<p>The fraud indicators and signals that triggered the suspicion were:</p> <ul style="list-style-type: none"> - Procurement: <ul style="list-style-type: none"> • Discrepancy (technical, quantitative and qualitative) between works carried out and technical specification set in the project documents, construction permit and construction work contract • Discrepancies between project indicators, results reported and actual results of the project • Missing documents in the public procurement files • Bidders submitted exact same offers, i.e. same mistakes,

	<p>same prices, same list of construction materials, same total budget as the project costs</p> <ul style="list-style-type: none"> • Same company delivered the designing of project budget at the time of project grant application and later the construction works • Inflated unit prices for construction materials and equipment items <p>- Cash payments:</p> <ul style="list-style-type: none"> • Missing audit trail concerning cash withdrawal and payments
<p>Description of fraud pattern</p>	<p>The project promoter implemented quantitative and qualitative changes to the project without prior approval from the Donors. This led to discrepancies between the original project implementation plan and what has been constructed, impacting on indicators and budget.</p> <p>In addition, collusion between bidders concerning the construction of sports facility took place. Offers were created by the same person using a software tool (floating coefficient) to provide different (higher) price of one of the bids by adjusting unit prices. Other manual interventions were performed into automated calculations.</p> <p>With regard to one of the payments to the service provider in charge with the construction of the sports facility, a bank transfer of 60,000 EUR was executed from the bank account of the project promoter to that of the service provider against the invoice issued by the latter. However, the bank, for the purpose of the investigation, issued a copy of the statement according to which no transfer of funds but a cash withdrawal has been made for the same amount. The bank statement submitted during payment claim verification was false. The statement provided by the project promoter was a payment order, not proving that the payment was executed. Neither the project promoter, nor the service provider could provide evidence that the payment was actually executed and received.</p>
<p>How the fraud was detected</p>	<p>Following allegations of fraud, the Donors of EEA and Norway Grants (i.e. Ministries of Foreign Affairs of Iceland, Liechtenstein and Norway) requested the Financial Mechanism Office (FMO) to launch ex-post audits on the project. The FMO sub-contracted an audit company to perform the said audits.</p> <p>The scope of the first ex-post audit was threefold, i.e. financial audit, procurement audit and audit of the systems controls related</p>

to financial controls. The main findings detected were:

- Discrepancies between results reported and actual results of the project. The Project Promoter did not achieve the project indicators and reported inaccurate information to the Focal Point. Moreover, the modification regarding the tennis courts was not incorporated in the Project Implementation Plan and can be considered as an unauthorized modification of the project
- Missing documents in the public procurement files and documents not disclosed to the auditors. The proposals did not contain all formal document required by the Terms of Reference. In addition, the cost breakdown for materials attached to the contract of Bidder 1 was exactly the same as the cost estimate prepared by Bidder 2 for the purposes of the public procurement proceeding, i.e. exactly the same prices were quoted for the particular items. Purchase of some equipment also showed price inflation.
- Following the check of major and/or unusual transactions on the Project Promoter's bank accounts the audit reported that many transactions of the Project Promoter are in cash – e.g. withdrawal of cash, cash payment, deposit of cash. It is not possible to identify the purpose of such cash withdrawals without having access to the corresponding invoices.

The said first audit was integrated by a second follow-up audit where the FMO requested to focus more on findings concerning procurement of construction works, technical inspection of the sports facilities and cash payments. Additional findings detected concerned:

- Construction of tennis courts and football playground were quantitatively (i.e. size of the courts and playground) and qualitatively (i.e. type of materials used and equipment bought) not compliant with the project contract.
- Public procurement documentation was not elaborated in compliance with the project documentation, the contract for construction was not concluded in compliance with the project documentation, the contract for construction works and the reality of works is not in compliance with the construction permit and the contract warranty period was shorter than what required by national laws.
- A bank account statement confirming the transfer in the amount of more than EUR 60,000 from the project bank account to the bank account of the contracted constructor, has been falsified. The amount mentioned on the bank statement had been withdrawn from the project's account in

	<p>cash. In this regard, a parallel investigation by the Anti-Corruption Office within Ministry of Interior was initiated.</p> <p>Following the fraudulent actions and the gravity of irregularities detected by the said two ex-post audits, the Donors accordingly decided to terminate the project and recovery the whole amount of project grant (EUR 668,184). Based on the case, follow up actions were put in place:</p> <ul style="list-style-type: none"> - Strengthening verification controls over projects with more emphasis on verification of reality of costs incurred - Incorporating an enhanced audit clause into all grant contracts with beneficiaries. This means that all beneficiaries have the obligation to contractually ensure that any auditing body has access to all suppliers' documentation, including accounting records - A procurement-wide audit was carried out in Slovakia for projects co-financed within the financial mechanisms 2004-2009 - Management and Control Systems for subsequent Financial Mechanisms 2009-2014 were improved, with a focus on financial verifications and procurement
<p>Weakness identified</p>	<p>The auditors recommended that the control system at the level of the Focal Point should be improved as for the following aspects:</p> <ul style="list-style-type: none"> - Strengthening verification controls at Focal Point over projects with more emphasis on verification of reality of costs incurred. - Considering the detailed findings of the audit and the consequences of irregularities already identified to potentially further investigate/inspect other projects in order to establish whether misuse of funds occurred. - Taking appropriate actions to decide on consequences of irregularities identified and potentially to be identified in case of more detailed review.